



DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

**STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL**

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

June 28, 2002

Governing Board
Nazlini Community Junior High School
HC 58, P.O. Box 35
Ganado, AZ 86505

Members of the Board:

We have reviewed the School's audit reports and Uniform System of Financial Records for Arizona Charter Schools (USFRCS) Compliance Questionnaire for the year ended June 30, 2000, to determine whether the School satisfactorily complied with the USFRCS.

As a result of our review, we noted significant deficiencies in internal controls that indicate the School has failed to comply with the USFRCS. In addition, the School lacked adequate accounting records and internal controls to enable its auditors to express an opinion on the financial statements.

To comply with the USFRCS, you must correct the deficiencies we have described in the enclosed summary within 90 days after the date of this letter.

Further, we have not received the School's audit reports and USFRCS Compliance Questionnaire for the year ended June 30, 2001, which were due March 31, 2002. We have also not received a contract for performing those audit services, and my Office must approve that contract before it is signed and any audit work begins. Nonetheless, the School must submit its fiscal year 2001 audit reports and USFRCS Compliance Questionnaire within 90-days to comply with the USFRCS.

During the 90-day period, the School may request a meeting to discuss its deficiencies with my Office and the Arizona Department of Education by calling Magdalene Haggerty, Accounting Services Director, or Michael Stelpstra, Accounting Services Manager, at (602) 553-0333.

A member of my staff will call the business manager in several weeks to discuss the School's action to correct the deficiencies.

Sincerely,

Debra K. Davenport
Auditor General

DKD/MH/ms

Enclosure

cc/enc: Ronald Arias, Principal

Nazlini Community Junior High School
Governing Board

Peach Springs Unified School District No. 8
Scott W. Thompson, Associate Superintendent for Finance and Information Systems
Arizona Department of Education

NAZLINI COMMUNITY JUNIOR HIGH SCHOOL

SUMMARY OF DEFICIENCIES

June 2002

Introduction

The State of Arizona provides educational opportunities for children through a public school system that includes charter schools. Each charter school has a governing board that is accountable to the school's students and their parents for the quality of education provided. Since charter schools receive state revenue, they are fiscally accountable to Arizona taxpayers and state officials. Nazlini Community Junior High School received state revenue of \$111,943 based on a student count of 30 for fiscal year 200001.

The foundation of the School's financial accountability is effective internal controls. Our Office and the Arizona Department of Education (ADE) developed the *Uniform System of Financial Records for Arizona Charter Schools* (USFRCS) to give schools the policies and procedures they need to maintain those controls. The policies and procedures set forth in the USFRCS incorporate finance-related state and federal laws and regulations and generally accepted accounting principles applicable to charter schools. Schools are legally obligated to comply with these policies and procedures, and following them is good business practice. However, we noted deficiencies that indicate the School has failed to comply with the USFRCS. We have described these deficiencies below and on the following pages, but have not included less significant deficiencies that have already been communicated to the School by its auditors for correction.

The School lacked adequate accounting records and internal controls

The School's auditors disclaimed an opinion on the School's financial statements due, in part, to inadequate accounting records and internal controls. As noted above, Nazlini Community Junior High School is fiscally accountable to Arizona taxpayers and state officials. A part of this financial accountability is the School's annual financial audit. The School must maintain adequate accounting records and internal controls to allow its auditors to issue an opinion on its financial statements. Such records and controls are also required by the USFRCS.

The auditor noted that the School's accounting procedures did not include adequate and timely review of transactions and adequate segregation of duties.

The School should assign duties among employees so that no single person performs all processes of a transaction cycle. Examples of appropriate segregation of duties are provided in USFRCS §VI, Accounting Procedures. A school administrator independent of the specific function should periodically review transactions/journal entries to ensure that each is made in compliance with the School's established policies and procedures. If the School is unable to adequately segregate duties due to insufficient staff size, it should implement an additional supervisory review at appropriate points in the process to help ensure that adequate internal controls are maintained. A lack of internal control subjects the School's resources to increased risk of misuse or theft.

The auditors also noted that the School did not have control over, and could not account for, its fixed assets.

Adequate control and accountability over fixed assets, which could represent a major investment of the School, should be established by developing a complete property control system as described in USFRCS §VI-E, Fixed Assets.

The School inappropriately used Bureau of Indian Affairs (B.I.A.) resources for charter school purposes

The School did not properly separate B.I.A. monies from the School's monies. The School used B.I.A. resources to pay its expenditures during the year ended June 30, 2000. In fact, the School used \$40,771 of B.I.A. monies to pay the bank overdraft reported in the financial statements. In addition, the School did not properly allocate joint costs between the charter school and the B.I.A. grant school.

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June 2002

The School should ensure that its monies are kept separate from the monies received from the B.I.A. B.I.A. monies should not be used for charter school purposes. Further, any costs that are shared between the charter school and the B.I.A. school should be properly allocated as expenses between them. If the School uses a formula to allocate expenses, the School should document the formula used and retain documentation to support the reasonableness of the allocation method used.

The School lacked adequate controls over student attendance reporting

The School did not maintain documentation that would verify the student attendance numbers reported to ADE. Since the School's state revenue is based on its student attendance, it is essential that attendance information be properly supported and accurately reported.

- The School did not accurately report memberships and absences on its 40th-day report. The School reversed the attendance numbers for grades seven and eight.

The School should have a second employee verify the accuracy of membership and absence days reported on its 40th- and 100th-day reports submitted to ADE. ADE's *Instructions for Required Reports*

- The School did not accurately report student attendance on ADE attendance reports. It subtracted absences from membership days causing its average daily membership (ADM) to be understated.

ADM is calculated as the total membership days divided by the number of days in session. A membership day is every day a student is enrolled in school and has not been withdrawn. ADE's *Instructions for Required Reports*

- The School shredded its withdrawal slips for fiscal year 1999-2000 prior to the audit.

An Official Notice of Pupil Withdrawal form must be completed and retained for each student who withdraws during the school year. The notice should be retained for 3 years after the fiscal year of withdrawal. ADE's *Instructions for Required Reports and Records Management Manual for Arizona School Districts*

- The School lacked documents to verify that its ADMS 40-2 and ADMS 45-1 reports were filed with ADE in a timely manner. Also, these reports were unsigned. In addition, the School failed to provide its CHAR 55-1 and CHAR 64-1 reports to its auditors.

The School must file the required reports with ADE within 12 days after the 40th- and 100th-day in session. The School should ensure that all reports are signed and that it maintains all supporting documentation. ADE's *Instructions for Required Reports*

The School failed to establish adequate controls over expenditures

The School did not obtain appropriate oral and written price quotations for its purchases. In addition, the School used the revolving bank account improperly. The School also did not prepare receiving reports and timely bank reconciliations.

- The School did not provide evidence of obtaining oral and written price quotations.

The School should obtain oral price quotations from at least three vendors for all purchases of at least \$5,000 but less than \$15,000. In addition, the School should obtain written price quotations from three or more vendors for all purchases of at least \$15,000 but not exceeding \$35,000. For any purchases of \$35,000 or more, the School should follow the School District Procurement Rules. USFRCS Memorandum No. 29

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- The School used its revolving account as a general bank account rather than a revolving account.

A revolving account should be operated on an imprest basis and should be used for activities that require immediate cash outlays such as postage, freight, fuel taxes, travel, and other minor disbursements. Salaries and wages should not be paid from the revolving account. USFRCS page VI-C-2

- The School did not prepare receiving reports for goods received.

To ensure that all items requested from a vendor have been received and to ensure that payment is made only for items received, the School should prepare receiving reports for all goods received, except exempted items. USFRCS pages VI-G-3 and 4

- The School did not reconcile its bank accounts in a timely manner.

The School should prepare monthly written bank reconciliations for each bank account. The reconciliation should be prepared by an employee not responsible for handling cash or issuing checks. Instructions for performing bank reconciliations are included on USFRCS pages VI-C-6 and 7.

The School did not maintain sufficient controls over payroll

The School did not use a delayed payroll system and lacked supporting documents in employee files.

- For two payrolls, the School did not delay the payroll process to help ensure that employees were paid only the amount actually earned.

The School should use a delayed payroll system which allows time for any necessary payroll adjustments. USFRCS page VI-H-1

- The School did not maintain all required supporting documents in its personnel files. A Form I-9 was missing from some files, and a W-4 was missing from one file. In addition, the Charter Centralized Personnel Records lacked employee background check and fingerprint records, employee compensatory time-off agreements, signed drug-free workplace policies, drug test results, and signed acknowledgements regarding employee conduct.

In order to provide adequate support for payroll expenditures and comply with federal and state law, the School should maintain the following documents in individual employee files: employee contracts or personnel/payroll action forms, employee eligibility verification (Form I9), employee's federal and state withholding allowance certificates (W-4 and A-4 forms), voluntary deduction authorizations, pay or position change notices, Arizona Revised Statutes §15-512(D) certification form, leave summaries, and direct deposit authorizations. USFRCS pages VI-H-2 through 4